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United States General Accounting Office

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Fact Sheet for the Chairman,
Subcommittee on the District of Columbia,
Committee on Appropriations, U.S. Senate

May 1988

DC GOVERNMENT

The Federal Payment to the DC Government Under Alternative Payment Methods



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May 5, 1988

The Honorable Tom Harkin
Chairman, Subcommittee on the
District of Columbia
Committee on Appropriations
United States Senate

Dear Mr. Chairman:

This fact sheet responds to your October 30, 1987, letter and later discussions in which you asked us to update table 5-1 in chapter 5 of our report, The Federal Payment to the District of Columbia: Experience Since Home Rule--Analysis of Proposals for Change (GGD-91-67, Apr. 23, 1981). Table 5.1, which is replicated in this fact sheet (see app. I), shows the actual federal payments for fiscal year 1980 and fiscal year 1981 and a projection of what the payment would be in 5 future years (fiscal year 1982 to fiscal year 1986) under certain payment alternatives. These alternatives included projecting the federal payment at the level as then authorized by legislation and determining the payment by using formulas that were based on (1) a percentage of the District of Columbia's (District) general fund revenue, (2) a cost-of-living escalator with an assumed rate of increase, and (3) the difference between the District's estimated future revenues and expenses.

You asked that we update table 5-1 to assist deliberations that may arise about changing the way the federal payment is determined. The federal payment is intended to compensate the District for the revenue foregone and expenses that result from its being the site of the Nation's capital. In determining the amount of the federal payment to request, section 501 of Public Law 93-198, the Home Rule Act, directs the Mayor to consider factors such as:

- tax revenue lost as a consequence of the limited commercial and industrial property in the District;
- the relative lack of taxable business income, which reflects the predominance of the public sector in the local economy;

- the net cost of providing public services for nonprofit corporations and businesses dealing exclusively with the federal government;
- recurring and nonrecurring costs of unreimbursed services provided for the federal government by District agencies and provided for the District government by federal agencies;
- expenditure requirements unique to the Nation's capital, such as extraordinary security measures and ceremonial functions;
- the tax burdens on District residents compared with tax burdens in surrounding jurisdictions and comparable cities; and
- the level of federal grants available to the District in comparison with other state and local governments.

The District has generally not requested a federal payment that is larger than the payment amount authorized by the Home Rule Act, as amended, at the time the request is submitted. The authorized federal payment was \$300 million in 1979 and was increased in 1984 to the current authorization of \$425 million for fiscal year 1985 and later years. Authorized and actual payments for the 10-year period fiscal years 1979 through 1988 are shown in appendix II.

Once the proposed federal payment is reviewed by the Office of Management and Budget it is submitted to Congress as part of the President's budget. The most recent federal payment, for fiscal year 1988, is \$430.5 million, which is slightly higher than the current authorized level. For fiscal year 1989 the President's budget is requesting appropriation of a federal payment of \$430.5 million.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to update table 5-1 of our 1981 report. In preparing the update, we obtained projections of the District's general fund current authority revenues¹ for fiscal years 1988 through 1991 from the District's Department of Finance and Revenue and actual general fund revenues for

¹Revenues limited to those which can be generated under current law, regulation, or other authority.

fiscal years 1986 and 1987 from the District's Comprehensive Annual Financial Reports. We also obtained total general fund revenue-expenditure gap projections for fiscal years 1989 through 1993 from the Mayor's fiscal year 1989 Operating Budget for the District.

To provide this fact sheet within the time frame you requested, we did not independently verify the accuracy of projected revenues and expenses, actual revenues, or revenue-expenditure gap projections. Using formulas similar to those in our 1981 report, we calculated estimates of the amount of the federal payment under several alternatives. We included a 24 percent of local revenues formula in our update of the table to provide a benchmark for comparing a formula based on the actual fiscal year 1988 payment to other payment formulas.

We discussed our approach for updating the table with the District's Associate Director for Economic and Tax Policy, who agreed with our presentation. Our estimates of the federal payment were prepared for the 5-year period fiscal years 1989 through 1993, which is the same period used in the District's multiyear budget plan in the Mayor's fiscal year 1989 budget.

Our work was done in accordance with generally accepted auditing standards from January through March 1988. The methodology used to prepare the updated estimates of the payment is described in more detail in appendix III.

SUMMARY

The updated version of table 5-1, table 1 on the following page, shows federal payments under various alternatives that range from \$425 million to over \$1 billion. The highest payments result from the use of a payment formula that is 40 percent of general fund revenues. The lowest payments are based on the currently authorized annual federal payment of \$425 million. Federal payments based on a 24 percent of revenues payment formula, which we derived from the fiscal year 1988 payment (the most current) as a percentage of fiscal year 1986 actual revenues, are closest among the percent of revenues formulas to providing the amount needed to close the District's projected gap between revenues and expenditures for fiscal years 1989 through 1993.

While the District's projected revenue and expenditure gap provides a basis for making some comparisons about the outcome of various formulas, closing this gap is not

Table 1:

Estimated Amount of The Federal Payment
to The District of Columbia Government
Under Alternative Payment Formulas
(Dollars in Millions)

<u>Type of formula</u> <u>or payment</u>	<u>Actual</u>		<u>Estimated</u>				
	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>
Existing or projected appropriation	\$444.5	\$430.5	\$425	\$425	\$425	\$425	\$ 425
Percent of local D.C. general fund revenues for second preceding year							
24 percent assuming no increase in tax rates			481	520	555	590	631
30 percent assuming no increase in tax rates			601	649	693	737	788
30 percent assuming local tax rate increases bring in 3 percent more revenue per year			619	669	714	760	812
40 percent assuming no increase in tax rates			801	866	924	983	1,051
Cost-of-living escalator applied to previous year's payment (4.5 percent per year)			450	470	491	513	537
Amount of federal payment required to pay 100 percent of projected gap between revenues and expenses			425	504	566	615	644

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necessarily a criterion for determining the federal payment. Rather, as outlined in the Home Rule Act, the costs and benefits associated with the federal presence in the District are to be the primary criteria to be considered in determining the level of the federal payment.

As arranged with the Subcommittee, unless you publicly announce its contents earlier, we plan no further distribution of this fact sheet until 30 days after its issue date. At that time we will send copies to interested parties and make copies available to others upon request.

If you have any questions, please call me on 275-8387.

Sincerely yours,

A handwritten signature in cursive script that reads "Gene L. Dodaro".

Gene L. Dodaro
Associate Director

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TABLE 5-1 OF OUR 1981 REPORT

Table 5-1
Estimated Amount of Federal Payment to the District
Government Under Alternative
Payment Formulas (note a)

<u>Type of formula</u> <u>or payment</u>	<u>Actual</u>		<u>Estimated</u>				
	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>
	----- (millions) -----						
Existing or projected appropriation	\$277	\$295	\$300	\$300	\$300	\$300	\$300
30 percent of local D.C. general fund revenues for previous year assuming no increase in tax rates			300	354	377	403	431
30 percent of local D.C. general fund revenues of previous year assuming local tax rate increases bring in 3 percent more revenue per year			300	365	389	415	444
40 percent of local D.C. general fund revenues for previous year assuming no increase in tax rates			300	472	503	538	575
Cost of living escalator (8% per year)			300	324	350	378	408
Amount of Federal payment required to pay 100 percent of projected gap between revenues and expenses			300	340	383	429	473

^aThe 1982 payment is not based on our calculations. It is from the District's 1982 budget submitted to the City Council in October 1980.

FEDERAL PAYMENT AUTHORIZATION AND
APPROPRIATION FOR FISCAL YEARS 1979 THROUGH 1988
(Dollars in Millions)

<u>Fiscal</u> <u>year</u>	<u>Authorization</u>	<u>Appropriation</u>
1979	\$300.0	\$250.0
1980	300.0	276.5
1981	300.0	300.0 ^a
1982	336.6	336.6
1983	361.0	361.0
1984	386.0	386.0
1985	425.0	425.0
1986	425.0	412.4
1987	425.0	444.5
1988	425.0	430.5

^aPayment amount differs from the \$295 million (actually \$295.4 million rounded) shown in table 5-1 of our 1981 report because in June of 1981 the District was given a supplemental appropriation to the federal payment of \$4.6 million.

METHODOLOGY FOR DETERMINING THE FEDERAL
PAYMENT TO THE DISTRICT OF COLUMBIA GOVERNMENT
UNDER DIFFERENT ALTERNATIVES

THE EXISTING OR
PROJECTED APPROPRIATION

Our update of table 5-1 shown on page 4 shows the actual federal payments for fiscal years 1987 and 1988 of \$444.5 and \$430.5 million respectively. For fiscal year 1989 and later years the table shows \$425 million, the currently authorized payment. The federal payments for fiscal years 1987 and 1988 were higher than the authorized amount because Congress appropriated funds exceeding the current authorization. The amounts of the payment authorization and appropriation for fiscal years 1979 through 1988 are shown in appendix II. For fiscal year 1989 the President's budget is requesting appropriation of a federal payment of \$430.5 million.

PERCENT OF REVENUES FORMULA ESTIMATES

The percent of revenues formula estimates for the fiscal year 1989 and later years' payments shown in the update of table 5-1 are our calculations based on the District's actual and projected local general fund current authority revenues for fiscal years 1986 through 1991 in table III.1.

Table III.1:

Actual and Projected Local General Fund
Revenues for Fiscal Years 1986 Through 1991
(Dollars in Millions)

<u>Fiscal Years</u>	<u>Actual</u>	<u>Projected</u>
1986	\$1,822.0	\$
1987	2,002.3	
1988		2,164.8
1989		2,311.0
1990		2,458.3
1991		2,628.2

Local District general fund revenues consist of income, sales, property and other taxes; license and permit fees; fines and forfeits; charges for services, interest, and revenue from other miscellaneous sources. Current authority revenue does not include revenue in future years if the authority has not yet been

enacted. For example, the Mayor's fiscal year 1989 Operating Budget proposes that 10 percent be restored as the top individual income tax rate for fiscal year 1989 and later years, rather than reduced to 9.5 percent as previously adopted. The additional revenue that would arise from the higher rate was not included in the projected revenues for fiscal years 1989 through 1991.

The actual revenues are from the District's fiscal year 1986 and fiscal year 1987 Comprehensive Annual Financial Reports. The projected revenues were provided to us by the District's Department of Finance and Revenue. We used the revenue projections in our formula examples without attempting to independently verify their reliability. Actual audited revenue figures, however, would be available to the District for use in such a formula at the time each year's District budget was being prepared. According to a Department official and the Mayor's fiscal year 1989 budget, this could assist the District in better predicting the federal payment. The Department of Finance and Revenue 1986 Annual Report states that, from fiscal years 1968 through 1986, its budget year revenue estimates have been within a plus or minus 1 percent of actual collections for 15 out of the 18 years. However, a Department official said that its estimates for years beyond the budget year can be expected to be less accurate.

We added to the updated table a formula that was not in table 5-1 of our 1981 report. This formula shows the most recent (fiscal year 1988) federal payment as a percent (24 percent) of the actual revenues for the fiscal year that precedes the payment year by 2 years. The 24 percent rate was the result of comparing the fiscal year 1988 payment of \$430.5 million to the audited revenues for fiscal year 1986 of \$1,822.0 million and rounding to the nearest full percent. This provides a benchmark for comparing a formula based on the actual payment to other payment formulas.

We based our estimates of the payment on the second preceding fiscal year's local revenues because they would be the most current actual amounts available at the time budget officials would calculate the payment amount to be included in the District's budget. For example, the estimated payments for fiscal year 1989 were the result of applying the percent rates to revenues for fiscal year 1987, which was an actual audited figure at the time the fiscal year 1989 payment amount would have been calculated.

The 30 and 40 percent of revenues formulas were included in our 1981 report and are included in this fact sheet because they are representative of proposed formulas. For example, the Mayor's

fiscal year 1988 budget statement to the Subcommittee on the District of Columbia, Committee On Appropriations, House of Representatives, proposed a formula that would set the payment at 35 percent of the second preceding year's local tax revenues. The percent of revenues formulas in the updated table show that the estimated payments under a 24 percent of revenues formula would provide more than enough funds in fiscal years 1989 and 1990 to close the District's projected gap between estimated revenues and expenditures but not enough after fiscal year 1990. The projected revenue-expenditure gap is shown in table III.2 and described more fully at the end of this appendix. As discussed on pages 3 and 5, however, under the Home Rule Act the criteria to be considered in determining the level of the federal payment to the District reflect the costs and impacts on the tax burden associated with the federal presence in the District and do not necessarily include the projected revenue-expenditure gap.

The percent of revenues formulas that use 30 and 40 percent rates would provide funds more than adequate to close the projected revenue-expenditure gap. In our 1981 report, in comparison, the 30 percent formulas did not provide funds sufficient to close the gap for all of the 4 years fiscal years 1983 through 1986. Our current example of a 30 percent of revenues formula provides a significantly larger federal payment than needed to close the gap because since our 1981 report the District's local revenues, which serve as the basis for our estimates, have grown. From fiscal year 1982 to fiscal year 1987 District revenues from local tax and nontax sources grew by 54 percent from \$1.3 billion to \$2.0 billion.

COST-OF-LIVING ESCALATOR

The cost-of-living escalator is based on the projection of a leading economic forecasting firm of the average annual increase in the gross national product implicit price deflator for fiscal years 1989 through 1993 of 4.5 percent applied to the actual payment in fiscal year 1988 and then to each previous year's payment. As shown in the updated table a cost-of-living escalator that would provide average payment increases of 4.5 percent annually through fiscal year 1993 would not provide sufficient funds to close the District's projected revenue-expenditure gap for the full 5-year period projected.

AMOUNT OF PAYMENT REQUIRED TO CLOSE REVENUE-EXPENDITURE GAP

The amount of the federal payment required to close the revenue-expenditure gap was calculated as the authorized federal payment

amount of \$425 million carried over through fiscal year 1993 plus the District's annual projections of the revenue-expenditure gap for fiscal years 1989 through 1993. For example, the amount shown in the updated table on page 4 for fiscal year 1993 of \$644 million is the projected gap of \$218.5 million rounded to \$219 million plus the authorized payment of \$425 million.

The gap is the difference between projected revenues and expenditures as shown in table III.2. The gap reflects revenue authority and spending policies proposed in the Mayor's fiscal year 1989 budget projected through fiscal year 1993 with revenues growing between 4.7 and 5.8 percent per year and spending growing between 6.3 and 7.5 percent per year. The gap for 1989 is \$0.0 because section 442 of the Home Rule Act requires that proposed budget year expenditures do not exceed estimated revenue.

The estimated revenues used to calculate the gap are higher than the local current authority revenues shown in table III.1 because the revenues used to calculate the gap include pending authority revenues, revenues transferred from the lottery and games fund, revenues from the sale of surplus property and federal contributions to the District such as the \$425 million authorized federal payment, a special federal payment to assist the transition of Saint Elizabeths Hospital from federal to District control, and other federal payments.

Table III.2:

Revenue-Expenditure Gap Projection
for Fiscal Years 1989 Through 1993

	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>
Revenues	\$2,847.7	\$2,980.7	\$3,145.2	\$3,320.6	\$3,514.4
Expenditures	<u>2,847.7</u>	<u>3,060.0</u>	<u>3,285.7</u>	<u>3,510.9</u>	<u>3,732.9</u>
Differences	<u>\$ 0.0</u>	<u>\$ (79.3)</u>	<u>\$ (140.5)</u>	<u>\$ (190.3)</u>	<u>\$ (218.5)</u>

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